

**ALASKA STATE LEGISLATURE
HOUSE RESOURCES STANDING COMMITTEE**

February 17, 2016

1:34 p.m.

MEMBERS PRESENT

Representative David Talerico, Co-Chair
Representative Bob Herron
Representative Craig Johnson
Representative Kurt Olson
Representative Paul Seaton
Representative Andy Josephson
Representative Geran Tarr

MEMBERS ABSENT

Representative Benjamin Nageak, Co-Chair
Representative Mike Hawker, Vice Chair

COMMITTEE CALENDAR

HOUSE BILL NO. 253

"An Act requiring the electronic filing of a tax return or report with the Department of Revenue; establishing a civil penalty for failure to electronically file a return or report; relating to exemptions from the mining license tax; relating to the mining license tax rate; relating to mining license application, renewal, and fees; and providing for an effective date."

- HEARD & HELD

PREVIOUS COMMITTEE ACTION

BILL: HB 253

SHORT TITLE: ELCTRNC TAX RETURN;MINING LIC. TAX & FEES

SPONSOR(s): RULES BY REQUEST OF THE GOVERNOR

01/19/16	(H)	READ THE FIRST TIME - REFERRALS
01/19/16	(H)	RES, FIN
02/15/16	(H)	RES AT 1:00 PM BARNES 124
02/15/16	(H)	Heard & Held
02/15/16	(H)	MINUTE(RES)
02/17/16	(H)	RES AT 1:00 PM BARNES 124

WITNESS REGISTER

JERRY BURNETT, Deputy Commissioner
Office of the Commissioner
Department of Revenue (DOR)
Juneau, Alaska

POSITION STATEMENT: On behalf of the governor, testified and answered questions regarding HB 253.

BRANDON SPANOS, Deputy Director
Tax Division
Department of Revenue (DOR)
Anchorage, Alaska

POSITION STATEMENT: On behalf of the governor, testified and answered questions regarding HB 253.

EDMUND FOGELS, Deputy Commissioner
Office of the Commissioner
Department of Natural Resources (DNR)
Anchorage, Alaska

POSITION STATEMENT: On behalf of the governor, testified and answered questions regarding HB 253.

ACTION NARRATIVE

[1:34:15 PM](#)

CO-CHAIR DAVID TALERICO called the House Resources Standing Committee meeting to order at 1:34 p.m. Representatives Talerico, Herron, Tarr, Josephson, Seaton, and Olson were present at the call to order. Representative Johnson arrived as the meeting was in progress.

HB 253-ELCTRNC TAX RETURN;MINING LIC. TAX & FEES

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CO-CHAIR TALERICO announced that the only order of business is HOUSE BILL NO. 253, "An Act requiring the electronic filing of a tax return or report with the Department of Revenue; establishing a civil penalty for failure to electronically file a return or report; relating to exemptions from the mining license tax; relating to the mining license tax rate; relating to mining license application, renewal, and fees; and providing for an effective date."

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JERRY BURNETT, Deputy Commissioner, Office of the Commissioner, Department of Revenue (DOR), advised that during this presentation the department will respond to various questions submitted during a previous presentation. He referred to the Alaska Department of Revenue, Tax Division, 2015 Annual Report, which is also provided online, and said that Brandon Stanos will speak to mining issues contained within the report.

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BRANDON SPANOS, Deputy Director, Tax Division, Department of Revenue (DOR), brought attention to the division's 2015 Annual Report. He explained that slide 5, "TAX RETURNS FILED by Tax Program during Fiscal Year 2015," shows the mining tax returns received, which is the number of volume of returns, and that corporate income tax receives more tax returns that can be electronic. He pointed to the mining license tax, shown in yellow, and said it accounts for 2.14 percent of all of the tax returns received.

MR. STANOS moved to slide 6, "STATEMENT OF REVENUES Listed in order of total amount Fiscal Year 2015," and said it shows the revenues collected and offers an idea of where the mining license tax fits into the picture of revenue received by the State of Alaska. Oil & gas production tax is the largest piece of the pie chart, and the mining license tax, shown in light blue, is 3.24 percent of all of the revenues collected by the Tax Division in fiscal year (FY) 2015. He noted that the revenues depicted in later slides do jump around from year-to-year. The mining tax is fairly unique in Alaska as it is based on the net income of the taxpayer, and other states tax by weight of the product, or by the sales, or by gross income. Mining tax has been around for a long time and, because it is based on the company's net income in a year, can vary from one year to another.

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REPRESENTATIVE SEATON inquired as to whether net income is an annual calculation. He further inquired as to whether the loss is carry forward to a future year or whether a loss or expenditure in one year is not further considered in the tax calculation.

MR. SPANOS replied that the mining tax specifically is an annual tax on a calendar year basis, or if a taxpayer reports fiscal

year federally then the taxpayer will report on a fiscal year. With regard to corporate income tax, there is a net operating loss carry back and carry forward. For the mining tax, if there is a loss in one year the company will not pay a mining tax that year, but there is no carry forward to another year.

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MR. SPANOS drew attention to slide 26, "Returns filed for FY 2015," and pointed out that it offers the description of mining tax and rates. He noted that the \$0-\$40,000 income bracket has no income tax and that the tax rate graduates with the net income level. Governor Walker's bill, HB 253, proposes an increase to the top bracket.

MR. SPANOS turned to the bottom of slide 27, "Tax Collections Information from FY2012 - FY2015," and noted the graph is "the meat of this part of the report for the mining tax." The graph shows the general fund, Constitutional Budget Reserve (CBR) Fund, and the tax collections. He explained that audits and assessments generally get transferred into the CBR Fund, and refunds from something that went into the fund also come out of that fund. Tax collections for 2015 were \$38 million in the mining tax, but they do fluctuate from year to year depending on the income reported on the tax returns for the state's taxpayers. He added that the pie chart shows how that fits into the overall tax collections, which is 3.24 percent of the total collections received in the tax division, and 96.76 percent for all others.

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REPRESENTATIVE JOSEPHSON requested Mr. Spanos to repeat his comments regarding the CBR Fund and how it works in conjunction with the mining tax.

MR. SPANOS answered that the CBR is for resource - mining, oil, and gas. He offered his belief that the Alaska State Constitution uses the word "disputed," but has been interpreted as an administrative proceeding. He explained that it begins as an audit or assessment in the form of a bill sent to the taxpayer, who has appeal rights. There's a due process and if there is a payment on an assessment it is transferred into the CBR if it's related to the mining tax.

REPRESENTATIVE JOSEPHSON observed that in FY 2015, \$38 million came in statewide in an uncontested way, and \$70,000 came in through an adjudication and disposition after an audit.

MR. SPANOS answered correct.

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MR. SPANOS turned to slide 27, "Returns filed for FY 2015," and advised that in FY 2015 there were 468 taxpayers and 616 tax returns. He explained that the tax returns included amended tax returns from previous years, which are counted as a return received in FY 2015. He noted that the mining tax is a license tax - a license must be obtained with the division before beginning mining operations, which then requires the company to file a tax return. In the event the company does not mine that year, it must still file a zero tax return with the division. He pointed out that many of those returns are under \$40,000 net income and the return shows no tax, but it does include information on the face of the return. Most of the division's information is confidential, although the licenses are public and available online. The information on the slide regarding credits is outdated, he said, as a couple more credits have been added against the mining tax.

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REPRESENTATIVE SEATON requested a more detailed explanation regarding the tax credits, how they are applied, and to the extent of how they can be applied.

MR. SPANOS responded that the Education Credit can be seen [on slide 27]. Additionally, there is the Film Production Credit that's available to take against the mining tax, as well as the Minerals Exploration Incentive Credit," which is also available online.

REPRESENTATIVE SEATON referred to the Exploration Incentive Credit under AS 27.30.010, which read:

(a) The commissioner shall grant to a person described in (d) of this section an exploration incentive Credit for the eligible costs of each of the following exploration activities that are performed on or for the benefit of land in the state for the purpose of determining the existence, location, extent, or quality of a locatable or leasable mineral or coal

deposit, regardless of whether the land is state-owned land:

REPRESENTATIVE SEATON noted that the Exploration Incentive Credit can be applied to any land within the state, whether state, federal, Mental Health Trust, or privately owned lands. He therefore asked whether the state is providing a tax credit where the state would not receive a royalty.

MR. SPANOS said he will get back to the committee with an answer.

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REPRESENTATIVE SEATON asked whether the Exploration Incentive Credit applies to all lands within the state regardless of whether the state owns them and whether the state receives any credit against tax. He said there was also a question about royalties for which he thought the answer was no. He expressed his concern that it applies under the statute to both the mining license tax and to royalties and during a tax year or a royalty payment period, so it appears that the 50 percent royalty or 50 percent tax applies to both royalty and to tax. He said he would like to receive some indication as to how these are applied because as he reads 27.30.050 it can be applied for 15 years carry forward but it doesn't have to be. It can be non-consecutive years, so it can be applied whenever the company desires for 15 years. And, he continued, it seems like that has \$20 million dollars, which has a large fiscal implication to the state's ability to receive revenue from any new mine, both revenue and tax, and if it's a credit against royalties, 50 percent of royalties, then it is also a question there.

MR. SPANOS answered that the credit can be taken against both royalties and tax, but there's no double-dipping. It can be taken against both in the same year if a company chooses, but the statute doesn't identify which one it must be taken against first. It is not like federal statute that often requires that the credit must be taken in a certain order against "this" first and then "this" second. For this particular credit, he continued, there is not an ordering, the taxpayer can choose to take it against the royalties or against the tax, but cannot take the same amount - the form that the taxpayer fills out starts to chip away at the credit and the taxpayer can only the credit once.

REPRESENTATIVE SEATON said that is how he read it, but said his concern is that royalty is the state's ownership interest and taking a tax credit against royalty actually means that the state is not only taking its taxing authority and reducing that, but also reducing the payment on ownership interest, or the payment on ownership interest. He said he would appreciate a discussion at a future time on the applicability of the Exploration Incentive Credit.

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REPRESENTATIVE JOSEPHSON asked whether the administration scrutinized AS 27.30 in advance of offering the mining tax legislation increase and whether reform was called for.

MR. BURNETT responded that he was not aware of any specific consideration to this, in that this Exploration Incentive Credit has been in place a long time and its existence is not necessarily an issue relative to the tax because the purpose of this is to increase the tax over time. It is not something that is looked at in terms of it reducing state taxes, but rather it is looked at as more of an incentive to produce more revenue in the future. He commented, "It's not a large amount of dollars that are actually been taken against our taxes."

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REPRESENTATIVE JOSEPHSON, relative to Representative Seaton's comments regarding using credits in places where royalty is earned and whether that is inconsistent with what is done on oil, said he thinks it's not. He pointed out that credits are offered on state land. Whether the policy should be different for mining versus oil and gas is worthy of discussion. He noted that credits are offered on state land where the state earns a royalty and asked whether Representative Seaton's view is that there should be a different policy for mining.

REPRESENTATIVE SEATON responded that normally on oil and gas there are oil and gas production taxes, but it generally doesn't apply to the royalty amounts. In this case, it is saying that it applies to the state's ownership amount, or can be applied to the state's ownership amount. He said that while the section of the statute is open, the committee should consider the implications for the State of Alaska, and whether that should be applicable.

REPRESENTATIVE JOSEPHSON said Representative Seaton clarified that this really is a different application as it is against the royalty interest itself.

MR. BURNETT referred to oil and gas production taxes and said the credits there apply on state and other lands. Although most of the production value is on state land, the tax credits would still be a credit against production from non-state land because the taxes are on non-state land as well, as long as it is produced within the State of Alaska.

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EDMUND FOGELS, Deputy Commissioner, Office of the Commissioner, Department of Natural Resources (DNR), said that with regard to questions previously asked, the committee was provided with two documents of information: "Alaska Mine Production Figures," which is a simple spreadsheet showing a five year lookback on all of the five major hard rock mines in Alaska, and the production of the commodities depicting the amount produced. He said there is also a five year lookback on the spot prices for those commodities. He then related that Trustees For Alaska v. State (1987) is the answer to Representative Hawker's question relevant to production royalties. He said, "The elevator speech condensation is that prior to this lawsuit we were not charging royalties for our mineral production; after this lawsuit went to the State Supreme Court we were forced to pass our law in 1989 that instead of the 3 percent royalty." There's a lot more in this lawsuit than just that, he added, but it deals with Section 6(i) of the Alaska Statehood Act, [Public Law 85-508, 72 Stat. 339, July 7, 1958].

REPRESENTATIVE JOSEPHSON requested clarification as to whether the state did not collect a royalty prior to instigation of the aforementioned lawsuit.

MR. FOGELS replied, "We had some kind of system where we were offsetting any kind of payments with annual labor and there was no formal royalty. And so, that was challenged ... and then now we have that royalty system in place."

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REPRESENTATIVE SEATON noted that the royalty itself was done by statute by the State of Alaska. He understood that it came up because the state had to do something and no one wanted to spend a lot of time because there were not many large mines at the

time. Therefore, 3 percent of the net operating just mirroring the tax was thrown as a placeholder until people would devote more time to an adequate royalty system. He asked whether this is Mr. Fogels' understanding as well.

MR. FOGELS replied he has not had the opportunity to look into the legislative history on that and therefore cannot comment as to how that number was derived or whether it was temporary in intention, or too high, or too low.

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REPRESENTATIVE SEATON said in moving forward, looking at the appropriateness of having a net income percentage representing the royalty as opposed to something based on point of production, or net smelter return, those kind of issues where the state was receiving a return for the state's actual minerals and not for someone's operating costs, and whether they are an efficient or inefficient operator would harvest the same amount, but it would very drastically change the state's royalty picture. He said he was laying the issue of "what's an appropriate royalty and an appropriate base for royalty" on the table, and encouraged the department to contribute.

MR. FOGELS responded that over the years he has been at DNR he has not been involved in any real hard discussions as to whether 3 percent was the right number, or whether the method of calculation was the right number. He opined that possibly part of the reason is that there is currently only one mine in Alaska that that production royalty applies to in any meaningful way. Pogo is the only mine currently on state land and there is not anything in the pipeline for a hard rock mine that will come on line any time soon on general state land.

REPRESENTATIVE SEATON explained his reasoning is that if the committee is going to make a change it should be done long in advance so the people know. He reiterated that the state is better off in considering whether the royalty is an appropriate calculation, and to put one in if it's not an appropriate calculation, so everyone knows the game way ahead of time.

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REPRESENTATIVE HERRON referred to the decision in Trustees For Alaska and noted that the number two plaintiff is from his region, and then there is the rest of them. He said, "It wasn't that this group of people necessarily were looking out for

everybody and figuring that the mining industry needed to pay a royalty." He therefore asked what was beneath that and whether it was because of fish versus mining.

MR. FOGELS said he is not familiar enough with the case to know the nuts and bolts of what drove it, but he was never under the impression that an environmental issue was a stake; his impression is that it was a fiscal issue.

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REPRESENTATIVE JOSEPHSON referred to page 4, "Proceedings Below," and said it describes that indeed this was about the plaintiffs' assertion that the state didn't follow Section 6(i) [Alaska Statehood Act] and needed to collect a royalty. He explained it wasn't a mining versus fishing dispute that was presented to the court.

MR. FOGELS replied that is his understanding as well.

REPRESENTATIVE HERRON said he brought up the point because he believes it is [a fiscal issue], but it is interesting that this group of plaintiffs would feel it was their responsibility to point out that Section 6(i) is not equitable across the state.

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REPRESENTATIVE JOSEPHSON, relative to the 3 percent and other major mining states, asked whether there is some comparable rate to the one-eighths that applies somewhat nationwide on oil fields. Setting aside deductions, and credits, and the like, he further asked whether there is a figure that other Rocky Mountain producer states are using that Alaska is not using.

MR. FOGELS answered he doesn't know because he has not spent a lot of time looking at royalties in other states since Alaska's land situation is vastly different than other states. He explained that some states don't have state lands, and some don't have the subsurface, so a comparison is apples and oranges for the most part. He said he is willing to spend more time looking into that if Representative Josephson desires, but said he is uncertain how much good information could be obtained that would be of use to the committee.

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REPRESENTATIVE TARR referred to the discussions regarding adjustments to the royalty rate or tax changes with regard to the mines in pre-permitting, such as Niblack and Bokan Mountain. She inquired as to when those leases are up for renewal and whether there might be an opportunity to make that adjustment at the time that those leases are up for renewal.

MR. FOGELS responded that Niblack and Bokan Mountain are on federal lands so the state would not receive royalty at all.

REPRESENTATIVE TARR posed an example of a mine located on state land and asked how it would work in terms of the timeline of when the state can actually make a change.

MR. FOGELS asked whether Representative Tarr is asking when could the state change the law to change the royalty rate for state lands.

REPRESENTATIVE TARR replied that that could be done at another opportunity, and clarified that she would like to understand the timeline on the leases, when the lease renewal would come up, and how any underlying changes would impact that process.

MR. FOGELS replied the 3 percent is in statute and doesn't change based upon lease renewals. There is no opportunity to change it other than by statute.

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REPRESENTATIVE TARR clarified she is trying to understand whether that would be a deterrent for someone at the time of lease renewal in terms of re-evaluating the opportunity. She asked whether that might be when the state might see something if people were going to depart from the activity they were engaged in right now.

MR. FOGELS suspected that once someone invests a lot of capital in a mine operation there is a lot of momentum there, and therefore the company is going to keep operating it as long as the economic conditions are favorable. There are probably a multitude of factors and the primary factor could be commodity prices at the time, and those factors will drive the company's decision whether to continue. The renewal of a lease or claim is an insignificant cost compared to operating the project. Even if a company had to temporarily shut down a mine, such as the Nixon Fork Mine, the company will probably keep its property

position legal and up-to-date. So, he continued, he doesn't think that would really have a bearing on this.

REPRESENTATIVE TARR surmised that the lease payments are so low relative to the opportunity that these changes are not going to impact the seven mines that are listed in pre-permitting and not operational while they make calculations about the financial viability of the project.

MR. FOGELS responded it is probably a very complex decision for the person holding the property. He noted that there are about 35,000 mining claims in the state and said people stake new claims and relinquish claims depending upon gold prices. People make economic decisions every year when considering whether they should maintain their claim position. He said he imagines that if there is some change in the fiscal structure for the state it would affect people's thinking on and some folks may be more inclined to shed their claim should the fiscal structure change.

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REPRESENTATIVE SEATON noted there are claims that are just being held without anything being done with the claim. He suggested that maybe the state would actually get more mines created if there is a 3 percent net smelter return royalty because the aforementioned owners would shed their claims and other miners would come in who would actually move forward and not just hold a claim. He described it as a hard nut to decide on, whether a small incremental amount that they have to pay the state is a net negative or a net positive because it may loosen up some of those claims and get those that are not going to be developed relinquished.

REPRESENTATIVE SEATON requested that the department supply the committee with what it knows about the other private royalties in the state. Mental Health Trust's are not secret and it is 5 percent net smelter return or gross amount on the value of the minerals, and there are mines occurring on Mental Health Trust lands, and private lands where it's 4.5 percent net smelter return. He said he would like to know the publically available royalty terms and basis for the operating mines to assist the committee in determining what the appropriate basis is. He suggested that if the appropriate basis for most of the existing mines to have up to 5 percent net smelter return, and the state is not availing itself of those same economic conditions that people go forward with and develop mines on, then it would seem that the state is leaving a lot on the table.

MR. FOGELS replied that he will find out what is publically available, but suspected that much of that is confidential negotiations between the mining operator and the land owner.

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REPRESENTATIVE JOSEPHSON asked whether Canada, a pro-mining country, uses a 10-15 percent net smelter return royalty or rate and further asked how that equates with the 3 percent mining license tax that Alaska uses on income. He said he is curious about the relative comparison of those.

MR. BURNETT noted that DOR provided the committee with reference material on Canadian mining taxes, and the materials may answer his question. If not, he said he will provide information.

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CO-CHAIR TALERICO expressed his appreciation for the efforts and information from the department in so far as it is nearly impossible to create head-to-head comparisons when they are all entirely different. He said one western state may charge a 5 percent net tax but have no corporate income tax or no royalty associated with the product, while others just have corporate income tax and not the net tax, and some are by tonnage. He opined that Alaska is structured entirely differently than most of the other western states.

MR. BURNETT replied that DOR has provided the committee with comparisons of states' severance taxes, as well as non-petroleum corporate income tax collections by sector for [Alaska] so it can be seen how each sector over the past several years has performed. He pointed out that the corporate income tax on the mines in Alaska in 2010 was a negative \$2.5 million but was \$81 million in 2011, which really looks at the commodity price worldwide and how it fluxuates. He said the department will provide the committee with whatever information possible to assist the committee in making decisions.

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REPRESENTATIVE SEATON requested an explanation of which credit or which application got the state to a negative income tax.

MR. BURNETT explained he cannot be specific as to each one, but corporate income taxes allow losses from previous years to be

carried forward. He said, "You're taxing on an allocation based on the company's ... U.S. income, so it is one where the loss could occur in Alaska, it could occur somewhere else in the previous year." All of Alaska's corporate income taxes are an allocation based on either worldwide or U.S. income.

REPRESENTATIVE SEATON inquired whether it is worldwide apportionment, but most of the mines were U.S.

MR. BURNETT offered his belief that the mining is U.S. income, and the oil and gas sector is worldwide.

MR. SPANOS added that there are sometimes very large amended tax returns that are refunds because a taxpayer may choose to change its method of expenses or some other claim. Normally the department will refund those and then audit that at a later period. So, it may be a large refund in one year, an audit, and a claim in the next year or a future year. Or, potentially, the taxpayer and department agree and so it remains as a refund.

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REPRESENTATIVE SEATON referred to the depreciation allowance used in mining and the shifting from cost depletion to resource depletion. He asked for an explanation as to how that affects the taxes.

MR. SPANOS said he would like to have the statute in front of him to provide details, but explained that there is a depletion allowance depending on what type of mineral a company is mining in that there is a set amount in statute for percentage depletion which, interestingly, can go over the actual costs, and then there is a cost depletion allowance which is usually used in the industry.

REPRESENTATIVE SEATON requested an explanation of what is depletion allowance and how it affects the taxes.

MR. SPANOS explained that the basic concept of depletion is that there is a mineral in the ground and the company is depleting that mineral, and the costs associated with getting at it so the upfront expenditures, similar to depreciation, is taking the costs off each year as the resource is depleted. In the event it is known how much is in the ground, such as coal, it can be depleted over the life of the mine. The statute allows for coal a specific percentage depletion, so it's not a traditional depletion method of saying it will last for 20 years and there

is this much and then a dollar limit is mathematically calculated to deplete each year. He offered his belief that the statute reads 10 percent, and that 10 percent is allowed each year regardless of how much depletion has actually been calculated on the company's books.

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REPRESENTATIVE SEATON posed a scenario of a hard rock mine with operational costs of \$50 million this year. He asked where the depletion comes into that and whether it wipes out the company's expenses or is in addition to expenses, such as the company has \$1 billion worth of minerals in the ground and will take 10 percent of that and these are the expenses, and the company takes another \$100 million of depletion and writes it off against its income. He asked whether the discussion is basically taking an additional reduction in profitability.

MR. SPANOS confirmed that it is in addition to the company's other expenses. He said depletion is its own line item expense that is used to calculate net income.

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REPRESENTATIVE SEATON said, "In our taxes we have cost depletion which means that you expect to spend the \$1 billion over 10 years, let's say, and so you'd take off \$100 million a year off what your income is before paying taxes, or you can do resource depletion which is after you've like used up 50 percent of the minerals that are estimated to be there, then you reduce your tax liability by 50 percent because you've used up 50 percent of the minerals." He asked whether that is the resource depletion calculation."

MR. SPANOS responded that he will get back to the committee with an answer.

REPRESENTATIVE SEATON stated he thinks the committee should have a presentation on how cost and resource depletion factor into the state's taxes. He opined that the state is losing a lot of the taxable income because it is written off - not only the expenses to get the net income and then there's either costs of resource depletion applied to further reduce the taxable income before paying taxes, and this could be huge portion. He offered his belief that Alaska is the only state in the nation that allows companies to switch annually from cost depletion to resource depletion depending upon which is more advantageous to

reducing the company's tax liability to the state. He reiterated that he would like the department to provide a slide presentation with graphics so the committee has an understanding when discussing whether the state is receiving its full revenue that is due under the statute because the statute includes this cost and revenue depletion allowance. He said that having an understanding of how that works in the real world would be helpful to him.

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CO-CHAIR TALERICO stated the committee won't ask for that immediately in order to give the department some time.

MR. SPANOS noted that Alaska is one of the only states that uses the net income tax liability on mining, so the depletion is usually a corporate income tax number and "we do piggy back the federal corporate income tax world" and the federal government is very strict about not allowing a company to jump from one method of depletion or depreciation to another. He related that the mining income tax is a very old tax and he does not know what the Internal Revenue Service code looked like back when the mining tax was brought on, but it is certainly a different world now. He said the department will put together a presentation that goes over the mining methodology.

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REPRESENTATIVE TARR referred to the Alaska mine production figures in the document provided by Mr. Fogels and said and recalled that one of her earlier questions was that people are trying to understand what impact the changes will have on future development opportunities. She observed that in 2013 Fort Knox almost doubled its production for that calendar year and inquired whether that increase was reflecting a high point in commodity prices or was due to some other reason.

MR. FOGELS replied that it could be a typographical error and therefore he will get back to the committee. However, he continued, such variations are typical and are based on a number of factors such as what is going on in the mine, the deposit itself, the kind of ore dug out, or issues with production. Typically a company is constantly trying to optimize its milling procedure and will find new ways to optimize to make it work better. A change in the chemistry of the rock is another factor that can cause things to change, or just the grade changes.

Every truckload of ore pulled out of a mine has a different concentration of the metal in it.

2:28:24 PM

REPRESENTATIVE TARR referred to the oil and gas tax credits and noted that a shortcoming in the legislature's work was that it didn't model things along the whole range of prices and the realities that are now being seen. Applying that thinking to consideration of the mining tax, she recalled Mr. Fogels saying that commodity price influences things more than any of the other underlying issues. Given the great fluctuation in commodity prices, she asked what resources are used by the department to look forward and make predictions about what the prices will be.

MR. FOGELS responded that, assuming a stable fiscal structure, commodity prices are probably the biggest driver for the mines. However, he advised, large changes to the fiscal structure could easily over-shadow any changes in the commodity price. A number of factors influence how much money a mine makes, with commodity prices probably at the top of the list. Other factors include fuel prices and the cost of rubber for tires. For example, Usibelli Coal Mine spends a lot of money on truck tires and that is a big cost driver in its operation. As far as what the department does, he said most of DNR's work is environmental with permits and regulating, so the commodity prices are not that big of a factor in DNR's day-to-day work. Where the department sees the fiscal side is in the production royalty. He reiterated that there is not an ongoing discussion of how to propose changes to that royalty structure based on what DNR sees commodity prices doing in the future.

MR. BURNETT added that for purposes of modeling for the fiscal note, DOR's economists have used the futures prices and markets rather than any kind of formal modeling for future commodity prices. He said DOR spends a lot of time on oil and gas prices and doesn't get those right either, but DOR tends to do as well as everybody else does.

2:31:46 PM

REPRESENTATIVE TARR commented that the \$6 million looks to be on the low side relative to some of the more recent years. She asked whether that was an attempt to not get it wrong and be over-optimistic of what that might be.

MR. BURNETT answered he did not make that estimate himself, but commodity prices have been declining across the board over the past several years. In 2014, the total income from the large mines that would be subject to this tax, the 13 taxpayers that were paying in the highest tax bracket, was \$561 million net income for tax purposes. He advised that \$6 million would represent about a \$300 million net profit for the largest taxpayers. That is certainly a difference in commodity prices and costs because the other thing that affects these is that costs of equipment and so forth have been going up at a rate faster than inflation. The department does have access to taxpayer confidential tax return information which is used for estimating future costs, et cetera. The department's economists look at a whole variety of things but that's the range of estimated net profits under the state's tax regime, which will vary widely year-to-year as it has in the past several years.

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REPRESENTATIVE JOSEPHSON recalled Mr. Burnett saying that the 2011 corporate income tax on hard rock mining was pretty sizable because commodity prices were high. Theoretically, HB 253 would generate about \$6 million of new income for the state. He asked how much [HB 253] would generate in a high-end commodity year and what the impact would be on the industry.

MR. BURNETT replied he believes that information may have been provided in a letter that came to the committee today.

REPRESENTATIVE JOSEPHSON confirmed that it was provided.

MR. BURNETT advised that the economist performing the modeling, Will Bishop, is in the room.

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REPRESENTATIVE HERRON asked why the proposed increase is from 7 to 9 rather than from 7 to 8.5 or 7 to 10.

MR. BURNETT responded that tax policy is for a variety of reasons. There was estimated income at various price points or tax rate points. This was discussed with a group of people within the administration, which included people from DNR and the Department of Commerce, Community & Economic Development, people familiar with the industry, and that's a decision that these people came up with. As to why that particular number, he said there's probably more art than science in some ways.

REPRESENTATIVE HERRON said that begs the question then - if a group of people threw a dart toward a target on the wall and that was the best shot. It seems that to increase the taxes on any industry there has to be a justification and an ability to articulate an understanding of the industry and that the industry can bear an increase. He suggested that drilling down and understanding the analysis will help in selling this tax to the legislature. It's important to legislators and industry to understand. He said it is important to be able to tell his constituents, as well as his own conscience, that it wasn't just a dart in a dart board.

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MR. BURNETT stated that the presentation is concluded and offered his understanding that there will be public and other additional testimony in the future.

CO-CHAIR TALERICO noted that Alaska's climate and the weather can create huge issues for mines, particularly open pit mines. For example, there was record-setting rainfall in 2013 where many of the mines were located. Also, any level of earthquake unnerves everyone working in underground mines and changes the way a person works for a while. Mining is an interesting industry that can be impacted with issues out of human control.

MR. FOGELS corrected the production figure for Fort Knox for the year 2013 - it should be 428.822, not 728.822. He said he will further verify the correct the number and send an amended document to the committee.

[HB 253 was held over.]

[2:40:23 PM](#)

ADJOURNMENT

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 2:40 p.m.